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No. 23

# Legislative Notice

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## **S. 949 – Taxpayer Relief Act of 1997** **(Revenue Reconciliation Act of 1997)**

Calendar No. 92

Reported from the Finance Committee June 20, 1997, by an 18-2 vote (Senators Nickles and Gramm voting no). S. Rept. 105-33.

### **NOTEWORTHY**

- The Majority Leader hopes to begin consideration of S. 949 on Wednesday. The Taxpayer Relief Act of 1997 (TRA) is the second of the two reconciliation bills provided for in H.Con Res. 84, the budget resolution of FY 1998. The agreement reached between Congress and President Clinton on May 2, 1997 is to balance the federal budget by FY 2002 and reduce net taxes by \$85 billion over five years and \$250 billion over ten years.
- TRA provides net tax reduction of \$76.8 billion over five years and \$238 billion over ten years. This makes it the *largest* tax reduction bill since President Reagan's tax reduction in 1981 and the *first* tax relief bill since President Reagan signed a tax reduction bill in 1986. The cost is more than offset by the economic dividend resulting from the balancing of the budget in FY 2002 — \$355 billion over ten years.
- TRA gives tax relief for taxpayers at every stage of their lives by providing a \$500-per-child tax credit, education tax relief, savings and investment tax relief, retirement tax relief, and estate tax relief. And, it returns to American taxpayers approximately one-third of the \$240 billion Clinton tax hike of 1993 — the largest tax hike in U.S. history.
- TRA is a first step to let taxpayers keep more of what they earn and is aimed directly at the middle class. Three-quarters of its benefits over the first five years go to those making \$75,000 or less, and nine-tenths go to those making \$100,000 or less. And, taxes for a family with two kids making \$30,000 would be cut by 50 percent.
- TRA, as a reconciliation bill, is afforded expedited treatment under the Budget Act. Further, TRA is protected under a unanimous consent agreement that prohibits raising a Byrd Rule point of order against the overall bill (see "Floor Procedure," pps. 8-10).

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## HIGHLIGHTS

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- **Tax relief for families and children:** A \$500-per-child tax credit for children under the age of 17 will take full effect in 1998, and will be available on a pro rata (\$250 for children under age 13) basis for 1997. (The President's proposed tax credit does not apply to teenagers. The Senate bill covers 11 million more children by covering teenagers.) Total family tax relief is \$83.9 billion over five years and \$187.7 billion over ten. (See, also, Chairman's Modification, below.)
- **Tax relief for education:** TRA includes President Clinton's HOPE scholarship proposal, provides for student loan interest deductions, permanent extension of employer-provided assistance, and expanded use of IRAs for education. Total education tax relief is \$32.5 billion over five years and \$81.7 billion over ten in TRA's Title II. However, when the Work Opportunity Tax Credit's extension (\$946 million over five years) and the requirement that the \$500 per child credit be used for children 13-16 for deposit in a qualifying education investment are factored in, the amount of education tax relief exceeds the \$35 billion stipulated in Congress' agreement with the President.
- **Tax relief for economic growth, savings and investment:** TRA provides a reduction in the capital gains rate, expanded use of IRAs for savings, and small business tax relief. Total tax relief in this area is \$7.4 billion over five years and \$50.2 billion over ten.
- **Tax relief for the next generation:** The confiscatory estate tax is reduced by phasing in an increase in the excluded amount from \$600,000 to \$1 million; a similar increase in the exclusion is given for farms and small businesses. Total tax relief in this title is \$6.5 billion over five years and \$37.4 billion over ten.
- **Revenue raisers:** Provisions include an extension of the airline ticket tax and numerous smaller provisions. Total revenue increase in this title is \$66.5 billion over five years and \$137.2 billion over ten. (See Chairman's Modification, below.)
- **Chairman's Modification:** Several significant changes were made in a chairman's modification. These include a **cigarette tax of 20 cents per pack** that will raise \$14.8 billion over five years and \$29.9 billion over ten. A modified version of the Clinton proposal for **continuous levy and debt collection** was also adopted and this raised (\$1.3 billion over five years and \$1.7 billion over ten). These additional revenues were distributed as follows:
  - reducing the burden of the airline ticket tax;
  - providing a portion of the child tax credit to individuals with no tax liability who receive the Earned Income Credit;
  - ensuring real estate receives a capital-gains rate reduction;
  - accelerating by one year the phase-in of estate tax relief; and
  - increasing by \$8 billion the amount of funding for children's health care.[See page 6 for further details.]

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## **BILL PROVISIONS**

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### **TITLE I. CHILD TAX CREDIT AND OTHER FAMILY TAX RELIEF (\$83.9 billion over 5 years; \$187.7 over 10 years)**

#### **1. \$500-Per-Child Tax Credit (\$83.5 billion from 1997-2002)**

- ▶ The Senate tax bill provides a \$500 tax credit for families with children under the age of 17, beginning in 1998. A \$250 tax credit is available in 1997 for children under the age of 13. The credit begins to phase-out for single taxpayers with adjusted gross income in excess of \$75,000, and for married taxpayers with AGI in excess of \$110,000. For kids age 13-16, the credit is available only if the amounts are contributed to an education savings account. A portion of the credit would be allowed for individuals with no tax liability and who receive the Earned Income Credit.

### **TITLE II. EDUCATION INCENTIVES (\$32.5 billion over 5 years; \$81.7 over 10)**

#### **1. HOPE credit for higher education expenses (\$20.4 billion over 5 years)**

- ▶ As proposed by the Administration, the Senate bill provides up to a \$1,500 tax credit per student per year for 50 percent of qualified tuition and expenses (but not room and board). Students attending a two-year community college or vocational/technical school would receive a credit equal to 75 percent of qualified tuition, for up to \$1,500. The credit phases out for individual taxpayers with modified adjusted gross income between \$40,000-\$50,000, and for married taxpayers with modified Adjusted Gross Income between \$80,000-100,000.
- ▶ As modified by the Administration, the HOPE tax credit is not contingent upon the student maintaining a "B" average.

#### **2. Student loan interest deduction (\$1.1 billion over five years)**

- ▶ Unlike the Administration's proposal, the Senate tax bill covers students who have just left school and face daunting amounts of student loan debt. The Senate bill helps these

individuals by providing an above-the-line tax deduction for student loan interest. The maximum deduction of \$2,500 would be allowed for interest paid on a qualified education loan during the first 60 months in which interest payments are required. The deduction is phased out for Adjusted Gross Income between \$40,000-\$50,000 for single filers and between \$80,000-\$100,000 for joint filers.

### **3. Education Savings Accounts**

- ▶ This provision follows S. 1, the Safe and Affordable Schools Act, introduced in January by Senator Coverdell and the Senate leadership to establish an education IRA, or savings account, to allow taxpayers to begin saving for their children's education. Taxpayers could contribute up to \$2,000 in nondeductible contributions per student into account. Up to \$2,500 could be contributed in such an account if a taxpayer received a \$500 credit for a child between the ages of 13 and 16. Interest accrued on amounts contributed to an educational savings account would be tax-free, and amounts distributed from an account to cover qualified higher education expenses would be excluded from gross income.

### **4. Private Pre-paid Tuition Plans**

- ▶ The Senate bill allows for the creation of private pre-paid tuition plans, similar to existing state plans. Eligible educational institutions would be allowed to set up pre-paid tuition plans that have tax-free buildup and allows for tax-free withdrawals when used for qualified educational assistance.

### **5. Other Education Provisions**

- ▶ The Senate bill provides tax-free withdrawals from state pre-paid tuition plans for qualified educational assistance, including room and board.
- ▶ Section 127, the current law exclusion for employer-provided educational assistance, set to expire on June 30, 1997, would be permanently extended. The exclusion would also apply to graduate-level courses.
- ▶ Repeals the \$150 million cap on 501(c)(3) bonds, to allow more bonds to be issued.

## **TITLE III. SAVINGS AND INVESTMENT INCENTIVES (\$7.4 billion over 5 years; \$50.2 billion over 10)**

### **1. Reduction of the Capital Gains Tax Rate (\$3.3 billion over 5 years)**

- ▶ The capital gains tax rate would be reduced from 28 percent to 20 percent for individuals in tax brackets above 15 percent. Taxpayers in the 15-percent tax bracket would have a rate of 10 percent. Depreciable real property would have a capital gains tax rate of 24 percent (reduced from 28 percent). The rate reduction would apply to taxable years ending after May 6, 1997.

**2. Expand Individual Retirement Arrangements ("IRAs") (\$3.3 billion over 5 years)**

- ▶ The Senate bill would increase the Adjusted Gross Income phase-out limits for deductible IRAs, so that by 2004 the phase-out range would double. Single taxpayers would have a range between \$50,000 and \$60,000, and joint taxpayers between \$80,000-\$100,000.
- ▶ The Senate bill would benefit homemakers by providing that an individual is not considered an active participant in an employer-sponsored plan merely because the individual's spouse is an active participant.
- ▶ Finally, the Senate bill would create a new IRA Plus account that allows taxpayers to make a nondeductible annual contribution of \$2,000. Qualified distributions from an IRA Plus would not be included in gross income.

**TITLE IV. ESTATE, GIFT, AND GENERATION-SKIPPING TAX PROVISIONS (\$6.5 billion over 5 years; \$37.4 billion over 10)**

- 1. Increase the Unified Credit (\$3.1 billion over five years):** Currently, the first \$600,000 in taxable transfers is exempt from the estate tax. The Senate bill would increase that amount to \$1 million by phasing in the increases over 10 years. Indexing provisions begin in 1999.
- 2. Provide an Estate Tax Exclusion for Family-Owned Businesses (\$3.1 billion over 5 years):** The bill would exclude from tax the first \$1 million of value in a qualified family-owned business, such as a small business or family farm.

**TITLE V. EXTENSIONS (\$6.7 billion over 5 years; \$7.2 billion over 10):** Four expiring provisions, including the work opportunity tax credit and the R&E tax credit, are extended.

**TITLE VII. MISCELLANEOUS PROVISIONS (\$5.2 billion over 5 years; \$9.1 billion over 10):** There are a number of miscellaneous tax provisions, the largest of which are:

- ▶ creating an Intercity Passenger Rail Fund to fund Amtrak (\$2.3 billion over 5 years);
- ▶ providing foreign sales corporation benefits for computer software (\$568 million over 5 years);

- ▶ expensing Brownfields redevelopment costs in empowerment zones, enterprise communities and EPA demonstration sites (\$247 million over 5 years)

**TITLE VIII. REVENUES (\$66.5 billion over 5 years):** There are a number of revenue offsets, the largest of which are:

- ▶ Extension and modification of the Airport and Airway Trust Fund excise taxes (\$34.3 billion over 5 years). Four separate provisions are included in this total (see details under "Committee Changes to Chairman's Mark," below).
- ▶ Increasing the tobacco excise tax by 20 cents (\$14.8 billion over 5 years; \$29.9 billion over 10).
- ▶ Require gain recognition on certain distributions of controlled corporation stock (better known as Morris Trusts) (\$1.5 billion over 5 years).
- ▶ Limiting net operating loss carryback period to two years and extend the carryforward period to 20 years (\$1.1 billion over 5 years).
- ▶ Extending the federal unemployment temporary surtax, which is set to expire in 1998, through December 31, 2007 (\$6.4 billion over 5 years).

**TITLES IX- XIII. SIMPLIFICATION PROVISIONS** [including provisions related to individuals and businesses; estate and gift taxes, excise taxes, and pensions] (These simplification titles amount to \$792 million over 5 years.)

**TITLE XIV. TECHNICAL AMENDMENTS** (No revenue effect)

### **Committee Changes to Chairman's Mark**

Two modifications to the chairman's mark were made just prior to the actual markup. The first contained six major provisions and the second contained 28 minor ones. The major ones are described here (some of which previously have been described in the title-by-title section above).

- Revenue raisers: A 20-cent-per-pack tobacco tax and a modification of the Clinton continuous levy and debt collection proposal were adopted. The tobacco tax raises \$14.8 billion over five years and \$29.9 billion over ten. Together they provided an additional \$16.1 billion over five years and \$31.7 billion over ten years.

- **Change in the airline ticket tax:** The 10-percent tax on foreign travel was replaced by a 10-percent tax on the domestic segments of foreign travel only. Additionally, an \$8-per-ticket departure tax was added. The combined effect was to raise \$2.8 billion less than was in the chairman's mark.
- **Real estate depreciation:** The capital gains rate on real estate depreciation recapture is reduced to 24 percent from the chairman's proposed 26-percent level. The current rate is 28 percent, providing an additional \$2.3 billion over five years and \$3.5 billion over ten.
- **Extension of per-child tax credit:** The \$500-per-child credit now will be available to some individuals who receive the Earned Income Credit (EIC) by allowing half of the EIC to be included before calculating the \$500 credit. This results in an additional \$2.3 billion over five years and \$5.5 billion over ten.
- **Estate tax unified credit:** The unified credit was accelerated by one year and will now reach a \$1 million exclusion in 2007.
- **Child health:** The \$16 billion included in S. 947 (the spending reconciliation bill) was increased 50 percent to \$24 billion over five years. This is four times what President Clinton's latest budget proposes. The additional money will be added into the Roth proposal that allows states to choose between Medicaid expansion or a block grant.

### **Amendments Adopted in Committee**

In addition to the Chairman's modifications, four amendments were adopted in committee and are described below.

- **Gramm:** Moving the receipts of the 1993 4.3-cent gas tax from the general fund to the Highway Trust Fund.
- **Mack:** Allow a one-time \$5,000 first-home-buyer Federal income tax credit for the purchase of a principal residence in the District of Columbia (expiring in 2002).
- **Grassley:** Extend and modify the current law partial excise tax exemption for ethanol.
- **Chafee:** Replace the current work opportunity tax credit with a two-tiered system.

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### **COST**

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Estimated Cost to the Federal Government, provided by the Congressional Budget Office: CBO concurs with the Joint Committee on Taxation (JCT) that the bill as reported would reduce governmental receipts by \$74.5 billion over the 1997-2002 period. In addition, CBO estimates

that the bill, including the committee amendment on child health, would increase direct spending by \$7.9 billion in FY99-02. Based on JCT estimates, CBO estimates that this bill would dedicate revenues of \$2.3 billion to the Intercity Passenger Rail Fund for the FY98-01 period.

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## FLOOR PROCEDURE

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### Some Quick Highlights For Floor Consideration of Reconciliation Bills

- The motion to proceed to the consideration of a reconciliation bill is not debatable.
- Per the Congressional Budget Impoundment and Control Act of 1974, as subsequently amended, floor debate on the Senate reconciliation bill totals 20 hours, equally divided between Republicans and Democrats.
- Time spent on quorum calls (unless preceding a vote) is counted against the debate time, but votes are not counted against the time limit.
- There is a two-hour time limit on all amendments offered in the first-degree; and that time must expire, or be yielded back, before a second-degree amendment can be offered to the pending first-degree amendment.
- There is a one-hour time limit on all second-degree amendments.
- Any debatable motions or appeals of the Chair's ruling carry a one-hour time limit.
- Time on all the preceding is equally divided, and is subtracted from the bill. In an ideal world, this would mean that proponents and opponents agree to use the same amount of time on each amendment or motion, up to the maximum allowed. But in the world of U.S. budget process, it also means that if proponents use one hour on a first-degree amendment, but opponents only use 10 minutes, then yield back time, the total time — 70 minutes — is equally divided, and 35 minutes are subtracted from the bill time on each side.
- If neither side yields time (i.e., if no one is conducting any business on the bill, but no quorum call is in progress), the Chair has the right to charge time equally from both sides.

### How To Tell If Your Amendment is in Order

Amendments to a reconciliation bill must be germane, otherwise a 60-vote point of order could be raised. Under the precedents of the Senate, germaneness is a more narrow concept than "relevance," which only requires a subject matter relationship. The following types of amendments are *per se* germane:

- Committee amendments;
- Amendments to strike;
- Amendments to change numbers or dates; and

- Non-binding amendments limited to matters within the jurisdiction of the committee of the reported bill; however, all amendments of this nature would violate the Byrd rule and be subject to a 60-vote point of order.

For any amendment that does not fall into one of the categories above, germaneness is determined on a case-by-case basis by the Parliamentarian. But, in general, the amendments:

- Must be relevant; and
- Must substantively restrict or limit some power, authority, duty, class, or other provision of the underlying bill or amendment.

All amendments must be offset and germane in order to avoid a Budget Act point of order. However, motions to strike are always in order.

Amendments are *not* in order to the reconciliation bill if they reduce any specific budget outlay below the level provided or if they reduce revenue increases below the level provided — unless the amendment makes a reduction in other specific outlays, an increase in other specific revenues, or a combination thereof that is at least equivalent to the outlay increase or revenue decrease in the amendment. Otherwise, the amendment would be subject to a 60-vote point of order.

## **Employing the Byrd Rule**

An amendment to the Budget Impoundment and Control Act enacted in 1985 offers some protection to reconciliation bills from the inclusion of “extraneous” material. This rule, named after its primary sponsor, Senator Robert C. Byrd (D-WV), applies the following rules (in addition to the preceding ones pertaining to germaneness) to remove material from a reconciliation bill when it is being considered on the floor. Under Byrd Rule procedures, it also applies to reconciliation conference reports. The Senate Budget Committee is obliged to report to the Senate a list of extraneous provisions.

If a Byrd Rule point of order against a provision in the bill is sustained, the offending provision is stricken from the bill. A waiver of the Byrd Rule requires 60 votes. Material is considered extraneous if it:

- Doesn't change outlays or revenues (unless it is a term or condition of a provision that does produce such a change);
- Increases the deficit *if* the committee has failed to meet its instruction;
- Is a provision from a committee which has no jurisdiction over the provision;
- Would produce changes in outlays or revenues which are incidental to the non-budgetary components of the provision;
- Creates a net outlay increase or a revenue decrease in the year following the scoring window (i.e., any year beyond FY 2002); or
- Affects the receipts or outlays of the Social Security trust fund.

## **Unanimous Consent Agreement Governing Consideration of S. 949**

On May 21, 1997, the Senate entered into the following unanimous consent agreement:

“Ordered, That during the consideration of [the revenue reconciliation bill] (and the conference report thereon), . . . [the revenue reconciliation bill] shall be taken together with all other legislation passed in the Senate pursuant to the reconciliation instructions ... [i.e., the Balanced Budget Act of 1997], when determining whether any provision of the [revenue bill] is extraneous . . .”

Translated, this means that the Senate may pass the bill by a majority vote of the Senate rather than 60 votes that would be required to waive the Byrd Rule.

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### **POSSIBLE AMENDMENTS**

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Due to the intricacy and importance of tax legislation, this bill is likely to be heavily amended. It is for this reason that such bills are rarely brought to the floor except under the protection afforded by the Budget Act's reconciliation process. It is not possible to give a comprehensive listing of the possible amendments but foreseeable ones are listed below.

Gramm/Nickles. Strike IRA deposit requirement for teenagers to receive the \$500 tax credit.

Daschle. Democratic tax substitute (similar to Gephardt's bill in the House).

Allard/Brownback. Index capital gains to remove the effect of inflation.

Craig. Institute a point of order against using tax increases to offset new mandatory spending.

Craig. Strike corporate registration provision giving IRS more power.

Gorton/Nickles. Reduce aviation excise taxes.

Lott. Increase the net tax cut to \$85 billion in order to comply with the budget agreement.

Graham. Reduce Hope scholarship tax credit to pay for school construction.

Allard. Strike the FUTA (unemployment) tax extension.

Conrad. Exempt Fannie Mae life insurance from COLI disallowance rule.

Jeffords. Strike the D.C. Investment incentive (except for \$5,000 first home buyer tax credit) and create a trust fund for District of Columbia school renovations.

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